RICHARD RUSSELL'S **DOW THEORY LETTERS, INC.**

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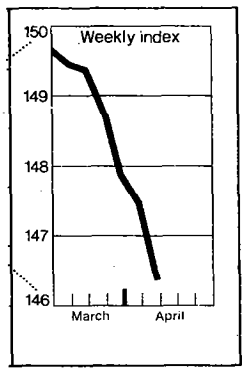
THE PICTURE: The American economic scene is turning from light gray to charcoal (not quite black yet). The March index of leading indicators dropped 2.6%, its 3rd steepest drop on record. We have a March 5.8% drop in construction outlays (sharpest drop since 1944), a .8% dip in industrial production, a 30% drop in auto sales, a 1.3% decline in retail sales, a 500,000 (April) fall-off in unemployment and on and on. The May 5 *Business Week* states that its widely-followed business index (see chart) "has been in a free fall for 6 weeks . . . preliminary signs suggest that April will be worse, maybe much worse."



This is the news that the stock market was probably discounting as it swooned during February and March. And it's one of the reasons why the Dow is now selling at only 6.5 times earnings. Many economists are now predicting a worse business picture than was forecast only a month ago, but nobody really knows. Economics, like oil prospecting, is still a matter of educated guesses.

As for what I expect, I'm sticking to my own crystal-ball predictions as outlined in the last few Letters. That is, I'm guessing that

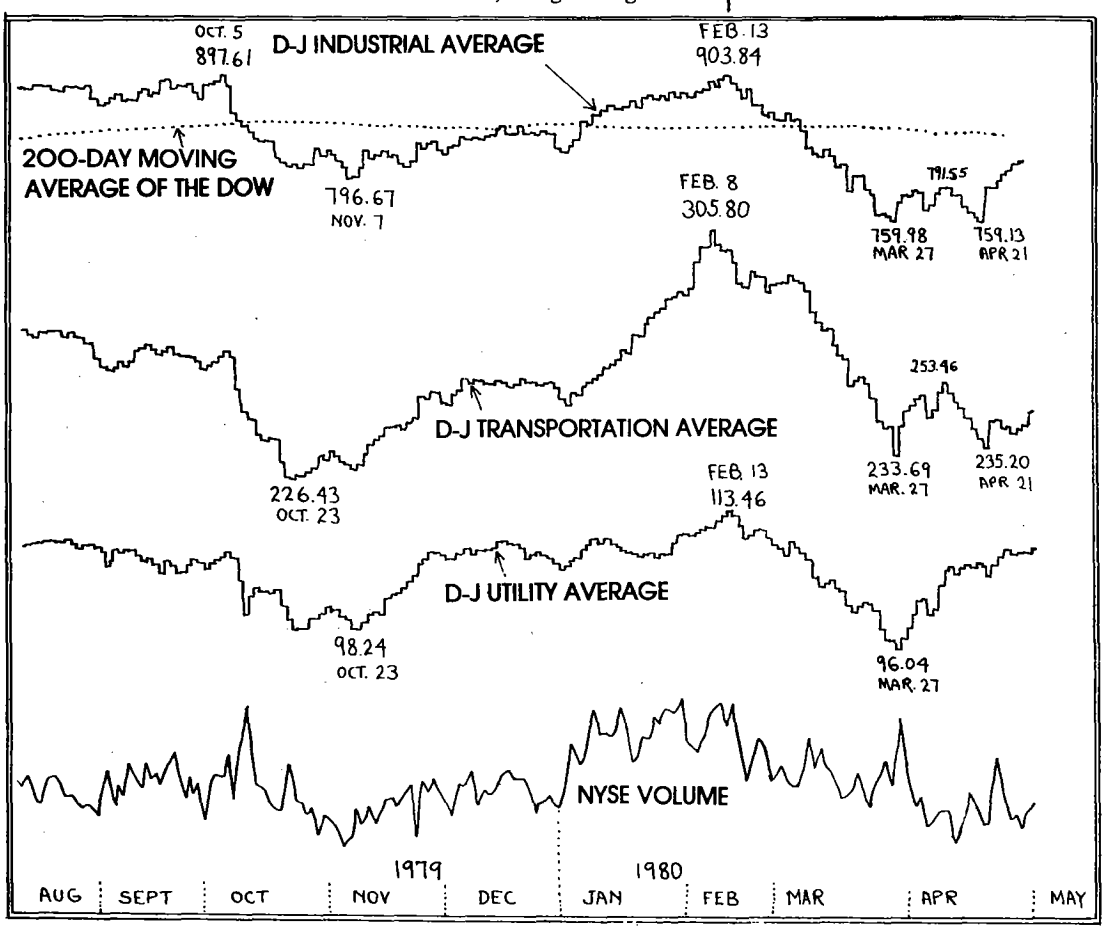
FRONT PAGE COMMENT: Alot of people are thrilled with this market rally, but I'm not one of them. Frankly, I'm more concerned with the coming storm than I am with the current market "pop."

What bothers me is the speed and violence with which this economy is tumbling. And above all, what bothers me is how this nation, in the face of a gathering recession, is going to service its $5.5 trillion in debt. We are at the stage now where the debt (like cancer) is taking on a life of its own. As business slows, as profits slide, as personal income drops, the burden of the current massive debt is going to increase at an exponential rate. Take autos. Ford has a funded debt of $1 billion. Already Ford is slipping into the red. Chrysler now has $1.28 billion in debt and is taking on more. If Chrysler survives, it will be a financial miracle. GM has just under $1 billion in debt. That debt should prove a burden soon.

The total servicing charge (cost of the debt) for all American corporations is now just short of $150 billion per year. The companies are not going to cover those massive services charges this year. And if the economic slump deepens (which I believe it will) we are going to see three developments: (1) dividend cuts and omissions, (2) bankruptcies, and (3) frantic moves by corporations to CUT COSTS. The quickest way to cut costs is to lay off employees. We're beginning to see that now, particularly in the auto and construction industries.

This nation is suffering from illiquidity on every level. The people and the corporations don't have enough quick assets (cash and equivalent) in relation to current liabilities. All of which adds up to plenty of drama in 1980. It should be one hell of a year.

Oh yes, from everything I read I gather that Carter, Volcker & Co. are supposed to panic shortly and open the floodgates of money. On this EVERYONE agrees. But the dollar is now turning weak, and it has already lost half its gains since the first of the year. Will everyone be right? Will Volcker throw in the sponge on the anti-inflation fight at the first sight of blood? I wonder.



the market was making an intermediate cycle-low around late-March (see last Letter, page 3), and that the bullish influence of the current up-cycle will exert its force on the market until around August. After that, it should be down, down and away again.

It's also true that the stock market was **heavily oversold** around the late-March lows. Even if the market is fated to collapse by late-1980, the oversold condition of late-March will have to be worked off. And that's exactly what I believe is occurring now; the market is simply working off an oversold technical situation. I have not been (and am not) optimistic about the chances of making big profits on this rally. I don't like the risk-reward situation, and I discussed that in the last report. Personally, I'm collecting 14% interest on most of my assets (in Treasury notes) and that's good enough for me in the current atmosphere. When the next MAJOR bottom comes along I hope to be able to catch it. Until then we sit on our hands and watch the show. We have many more scenes to go before 1980 breathes its last.

THE MARKET: From the standpoint of classic Dow Theory, the near-term picture is one in which the Averages are "disagreeing." This is known as divergence, and since late-April we have seen two examples of divergence; divergence on the downside (which is bullish) and divergence on the upside (which is bearish).

Note on the page 1 chart that the Industrials recorded lows of 759.98 on March 27 while on the same day the Transports recorded a low of 233.69. Here a brief rally then took Industrials to 791.55, Transports to 253.46. A second decline then occurred. On this decline Industrials broke to a new low of 759.13, but Transports refused to confirm (Transports on April 21 held at 235.20, better than 2 points above their March 27 low).

This non-confirmation set the technical conditions for the rally since April 21. But the striking thing about the rally is that the Transports have consistently refused to confirm the Industrials.

Note on the chart that Industrials have pushed well past their April peak of 791.55. Yet the Transports have halted better than 10 points below their comparable 253.46 April high.

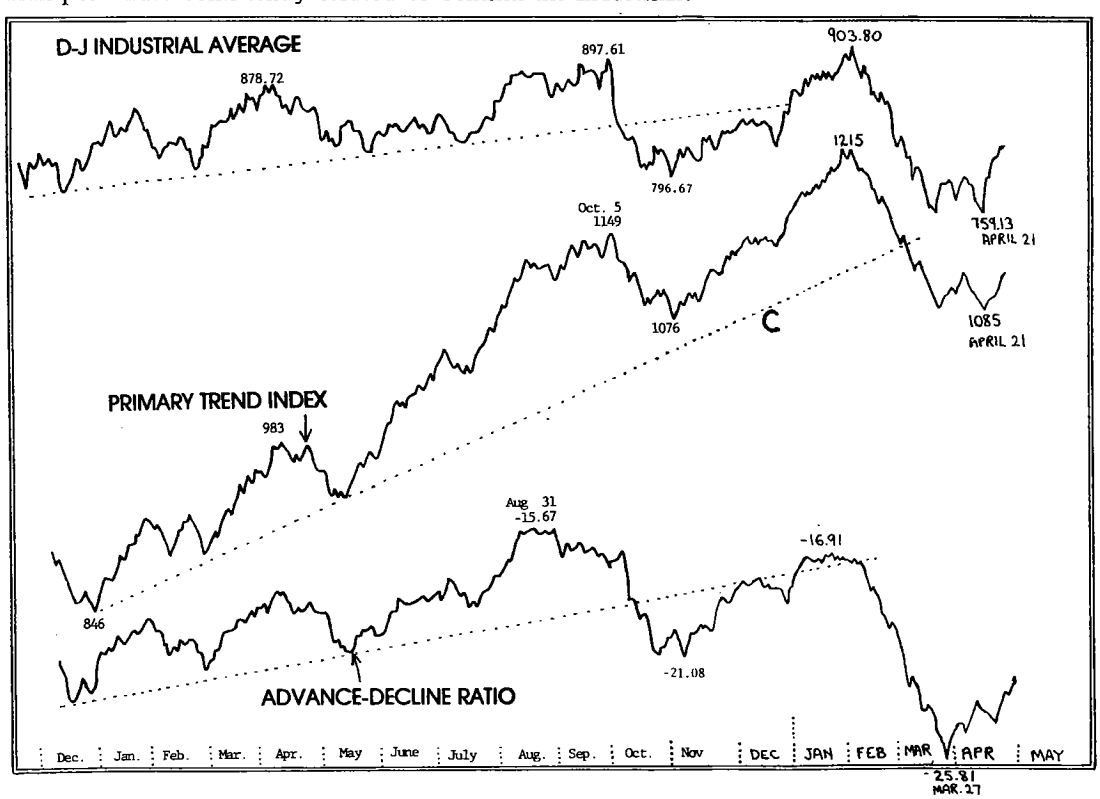
According to Dow Theory, the two Averages must confirm each other through preceding points. If they don't, then the validity of the move must be questioned, and one must be on guard for a reversal. Therefore, just as the downside non-confirmation of April 21 set the stage for a reversal to the upside, the upside non-confirmation now in progress could be setting the stage for a reversal to the downside.

Turning to the chart of the Primary Trend Index (PTI) and the A-D ratio, we have a mixed picture here too. The PTI hit a low of 1085 on April 21, and it has been behaving sluggishly ever since. So far, I'd have to call the action following March 27 just sideways movement. I'm still waiting for a recognizable trend.

The A-D ratio, however, has pushed up rather steadily. It hasn't been a spectacular advance, but the A-D has recouped about 1/3 of the losses sustained during the January-to-March smash. The A-D rise has, of course, been helped greatly by the drop in interest rates (since about 1/3 of the stocks on the NYSE are interest rate sensitive).

PTI, LONGER-TERM SIGNALS: No market indicator is infallible, the best work a majority of the time. The indicators that I have found to be most successful are the ones that require interpretation. Any fool can follow a mechanical index that provides mechanical signals. But fools don't survive long in the markets.

Back in Letter 777 (February 27) I wrote that the PTI for the first time had not confirmed a new Dow high. "This action reflected some minor weakness," I stated, "and constituted a minor sell signal." I then drew attention to the PTI trendlines, noting that the first trendline was close to being violated.



In Letter 778 (March 12) I noted that major trendline C on the PTI had been broken, and "I take this as a signal of longer-term weakness." In a recent Letter (779) (March 26) I noted that "the PTI has now broken below all rising trendlines of the past 2 years, and the possibility of a new major declining trend in the PTI must be conceded." Letters 778 and 779 advised that all investments be switched to Treasury bills. So far, the PTI has kept us out of trouble; in many cases it has helped subscribers to avoid huge losses.

I have written many times that a major rising trend in the PTI may not help all stocks, but no major market slide can materialize while the PTI pushes higher. Furthermore, periods in which the PTI records successive highs

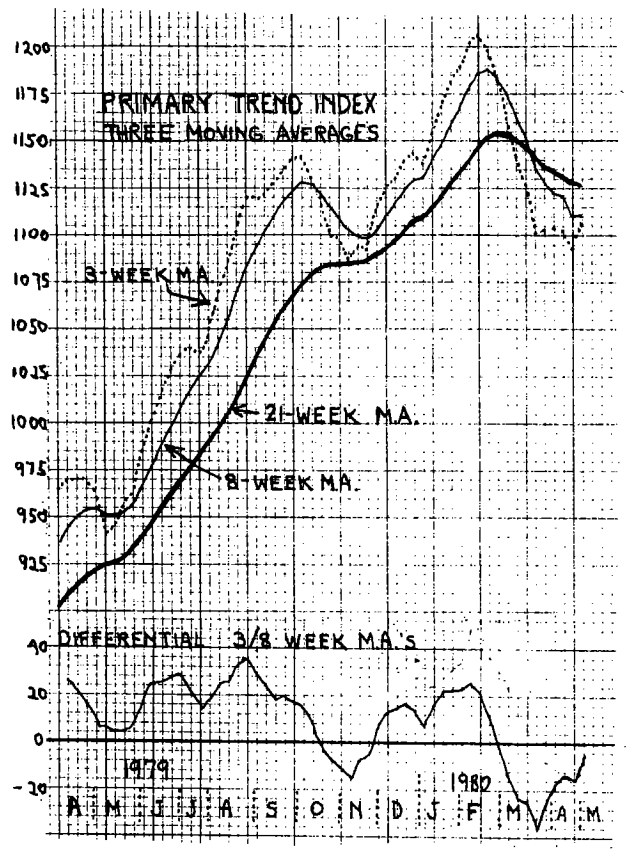
are almost always profitable for investors in common stocks. Obviously, the converse is true when the PTI is in a major downtrend.

I invented the PTI in 1971, and I have computed it and tracked it on a daily basis ever since. For 9 years I have interpreted the PTI on the basis of trendlines, successive highs or lows and whether the PTI confirms or fails to confirm the Dow. In early 1979 I decided that it might be helpful to run the PTI on the basis of three moving averages, a 3, and 8 and a 21 week MA (all computed on an exponential basis).

I am including my chart (page 3) of the 3 MA's in this Letter for the first time. At the bottom of the chart is a differential line showing the difference in points between the 3-week and 8-week MA's. By construction, this line must lead the much more important signals given when the 8-week MA moves above or below the 21-week MA.

The sensitive 3-week MA broke below the 8-week MA on the week of February 28, and this suggested that trouble was brewing (note the differential dropping below zero). On the week of March 28 the 8-week MA broke below the 21-week MA. This was a major bearish signal for the PTI. And it means that the market is now beginning to evidence important technical deterioration (note that during the late-1979 market "Massacre" the 8-week MA never dropped below the 21-week MA).

Current Reading: The 21-week MA is now trending down, something it has not done in over a year. The 8-week MA is below the 21-week MA, so the two MA's are now in the bearish position. The very sensitive 3-week MA has been responding to the latest market rally, and the differential (difference between the 3 and the 8-week MA's) is moving back towards the zero level.



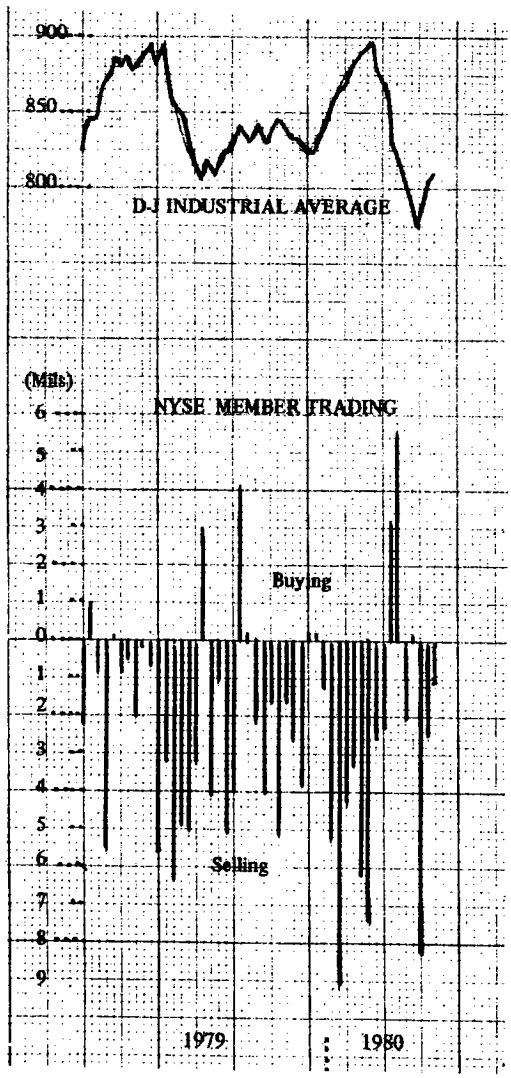
From the interpretive point of view, I am wondering if the 3-week MA (dotted line) is now in the process of forming the right shoulder of a head-and-shoulders top formation. If so, it seems to me that the formation should be completed around July. This would mean major trouble for the market during August and thereafter. It's a fascinating study, and we will need patience as we await the full story.

* *

As an aside to the current market picture, I want to include my chart of the weekly transactions of the NYSE members. This chart shows the buying or selling differentials of the Exchange members during each weekly period since July, 1979. I feel this study is instructive.

Normally, the members sense a coming market top or bottom, and they do their buying or selling in advance. Thus, prior to a major top the members will cut back on their buying, then step up their selling near or at the major top. The reverse is true near major bottoms. At such times it is usual to see the members cut back on their selling, then step up their buying markedly as the market heads into the final bottom area.

In other words, in a bottoming area, it is normal for the members to be accumulating shares and this can be seen by a preponderance of buying balances.



We have seen no such accumulation area in the members' statistics during 1980. Note that during 1980 so far there have been only two weeks of real buying while all the rest have been selling areas.

This study does not imply that the market cannot now rally (which it has been doing), but it does tell us that the members have been selling right through the rally. This casts doubts on the quality and the staying power of the April-May advance. It's not one that I want to jump in to.

SHOCKER: Last week I had a lengthy visit from my friend Mr. X. X for many years has made his living by gathering, collating and analyzing information from the entire defense establishment (from NASA to the Dept. of Defense, from the various "think tanks" right down to the defense suppliers and prime contractors). In a phrase, he knows from whence he speaks. What X told me last week was a shocker, and I wanted to relay it to my subscribers. I have seen this information published NOWHERE ELSE.

Russell: Mr. X, I'm a market man, and I believe what the markets are telling me. Right now the defense stocks are not acting well. Many have reacted severely over the past month, which is surprising and mystifying in view of the big defense build-up which we are told is developing. What do you make of this?

Mr. X: You've heard right, you've taken in what Washington has said, but what Washington has said does not jibe with what is happening and what is going to happen. The facts are that the Carter Administration is trying to get our allies to share or help in the military defense of the West. This may work, but so far I have seen nothing to suggest that it will work. As far as the US is concerned, we will be spending less on research & development (R&D) and we will be spending LESS on defense in 1981 than in 1980. According to my tabulations and statistics, the cyclical defense industry is probably at a high here in 1980. I see defense spending actually dropping 5% or more in 1981, and I don't care what Carter tells you!

Russell: How can that be? Are we being lied to?

Mr. X: Lied to? I don't deal with morality, I deal with facts and conclusions based on facts. Look, this Administration proposed a $155 billion defense budget. Fine, but that budget then has to go to Congress, and the money has to be appropriated. Fine again, but then that money has to be SPENT. And here's the catch. None of the prime contractors such as Boeing, General Dynamics, McDonnell Douglas, Grumman, Rockwell, are increasing their square footage in their plants. Now when you are on three shifts (which they are) and you don't increase your square footage of plant area, you're not going to increase your capacity. You're at your production limit. And that's where the major contractors are.

Russell: I don't understand. Why don't they increase their footage with all these contracts coming down the line?

Mr. X: Ah, you see the contractors have been through this before. Back in 1970 they geared up and they were hung high and dry. Do you remember the famous sign at Boeing? "Will the last person leaving the factory please turn out the lights." The prime contractors have looked at the Carter 1981 budget, and on the basis of that, they are not spending. And that means that regardless of appropriation, they are not going to produce more. The money is not going to be spent. They're producing all they are going to produce–now.

Russell: What about R&D? What's happening there?

Mr. X: That's the most disheartening and ominous part of it. R&D is lagging badly. I see nothing to indicate that we are even attempting to catch up to the Russians. You see, R&D is the key to the future. Ultimately, everything stems from R&D. R&D is vital to any enterprise, whether it's a corporation, a think tank, a scientific enterprise or the defense department. This is where the ultimate leadership must start.

Unfortunately, the Russian military superiority, based on what I see in our R&D, should **gather impetus**, widen in favor of Russia. For instance, we are coming out with a new tank. But the Russians have a tank on the field which is in almost every way superior to our new tank. The US tends to modify, not bring out new concepts. Thus we will have a model XM-1, then an XM-2, then XM-3 and on and on. In the end, all our XM's will be antiquated including the latest modification.

Russell: What are we doing in the way of new missiles or new aircraft?

Mr. X: I repeat, I see nothing to remotely suggest that we are attempting to close the gap or the Russian lead in this field. The gap is actually widening, this is the operative fact.

Russell: All right, but then what's on Carter's mind? What is he thinking about?

Mr. X: What isn't on Carter's mind is the military. As you know, over the last 6 months the military has come into vogue. Everybody now knows about the Russian lead. There was a great hue and cry to "catch up." Carter, in his waffling way, has resorted to cosmetics, but I feel that accomodation to the Russians is really Carter's way. Carter avoids all military confrontations, he tries to avoid all shows of force. Perhaps he believes in the Tri-Lateral way, perhaps he believes that pulling the West out of the Olympics or a Western cut-off of grain can force the Russians into a peaceful stance. I don't really know what he's thinking, but I do know what Carter is not doing, and he's not putting forth any plan to build up the military. And that's why the defense stocks are acting so listlessly or even reactionary in the face of supposed "good news" on the military "build-up." There isn't going to be any military build-up! Furthermore, military contracts are now being stretched out, slowed as to delivery!

Russell: It's really a shocker. You know, Carter is the first President in modern history to go into an election with auto sales lagging, housing collapsing, high interest rates and a reeling economy. Now you tell me that the defense budget will not offer any plusses either!

Mr. X: Defense spending will remain high, but it will NOT offer any stimulus from here on–none at all. In fact, I would say that it will be a letdown, because defense spending will fall short of market expectations.

To sum it all up, Russell, I believe that Carter has already settled for a US that is number 2 in military strength in the world. He evidently believes that the US cannot or cannot afford to catch up with the Russians. Perhaps he feels that catching up is not necessary.

For whatever reasons, I can tell you that the US is falling further behind the Russians militarily, and that defense spending will be a disappointment to those who believe that parity with the Russians on a military basis is essential. Your defense stocks obviously suspect that something is wrong. I've now told you what is wrong.

Russell: My last question is, do you think that Europe and Japan together with the US will be able to keep parity with Russia militarily? Can the so-called Tri-Lateral concept work?

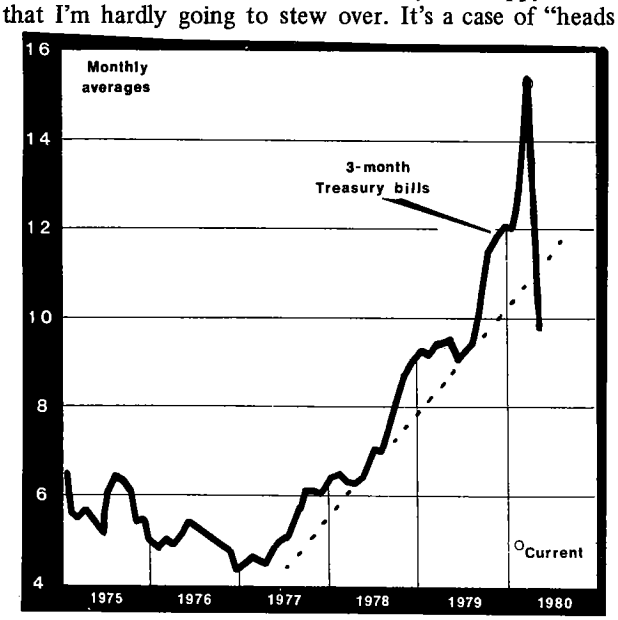
Mr. X: Conceivably it could work, but in actuality it is not working. The Russians are pulling far away from the West (and Japan) as a whole. And ironically, even as you write this, Western corporations are competing with themselves in selling Russia vitally needed scientific supplies, factories and concepts. I believe it was Lenin who supposedly said, "When we hang you capitalists, I fully expect you to fight among yourselves for the privilege of selling us the rope."

BONDS, MONEY: Those of us who purchased the two-year T-Notes or 5-7 year T-Bonds as recommended in Letter 780, p.1, now have to deal with one of the pleasantest of all investment decisions. Should we sit and collect 14% on our money into 1982 or should we "take the profits and run"? Honestly, I have no strong feelings either way, but I'm tempted to sit a while longer with my 2-year Notes.

The explosion in money instruments and the collapse in interest rates has been one of the most spectacular in Wall Street history. Many of the Notes are up as much as 5 points, longer-term T-Bonds are up as much as 16 points ($160)! Day after day the experts predict a top on the money instruments; day after day traders sell and sell short–and the money instruments keep on climbing.

My own guess is that the 91-day bills (the bellwether of short-terms) could hit yields as low as 8-9%, then interest rates could reverse violently and rally to recoup maybe half the ground lost. Thus, **traders** might start thinking of moving out of the Notes and back into T-bills again–all in the hope of a second ride on the interest rate train.

As I said before, the choice either way is a happy one and one that I'm hardly going to stew over. It's a case of "heads I win, tails I win" and it's pretty much up to each individual subscriber whether he wants rapid-fire profits now or another two years of 14% interest return. One answer, of course, is to take HALF profits now and hold the remainder.



What I will probably do is sit a while longer, and if shorter-term interest rates sink too far too fast (say 8% on 91-day bills), I'll sell my Notes and take the profits (I'll switch back to 91-day T-bills).

NOTES & QUOTES: I have noted in the past that one characteristic of a primary bear market is that during the bear market "nothing seems to go right." Or to put it another way, whatever can go wrong (during bear periods) does go wrong." To my mind, this is the meaning of Jimmy Carter, his very presence in the White House, and his uncanny, never-ending stream of "bad luck." Of course, the latest Carter escapade (the ill-fated Iran rescue attempt) would have been acceptable 4 or 5 months ago But the timing of the event was disastrous. If ever an escape attempt was slated to fail, this was it. What with crashing choppers, American dead left where they lay, rescue plans left in the plane, charred bodies strewn over the sands, it's a tragic commentary on US capabilities. And I ask myself, "Why the devil didn't they send in 25 helicopters, why did they call it so closely, why did they panic to leave the scene, why were our dead left on the ground, why, why?"

The depressing answer is provided by William Safire in a recent column. It's the same old story. In the face of emergency, Carter waits as long as possible and then responds with as little as possible. A few paragraphs from the Safire column are included below:

In fact, the reason the rescue failed was not that one helicopter pilot lost his way, but that the conception of the raid was not bold enough: The President wanted so much to make his surgical strike bloodless that he could not make the incision. By reducing the risk of loss of life, he increased the risk of failure of the mission, and the tragic irony came when lives were lost after his decision to retreat.

Months ago, the original plan called for a 350-man force, conveyed by many small choppers, supported by fighter-bombers. This was scrapped not because it was considered foolhardy — as we now know, the publicly derided rescue mission was secretly believed to be possible — but because it would have cost some American lives and probably Iranian lives.

Carter could not deal with that and called for a "safer" option. The scaled-down plan finally adopted — 90 men, with eight helicopters straining technical capabilities — was attractive to him because it could be canceled along the way. Much emphasis was put on the bailout points; military strategist Edward Luttwak calls that "deciding to get married and concentrating on divorce arrangements."

By convincing himself of the "humanitarian" side of the operation, the President rationalized his minimalist approach to the combat side. That was one reason he did not consult with Congress under the War Powers Resolution: Not only was he not making war, he was seeking to avoid combat.

That hope of exerting military power without violence vitiated the commando spirit so necessary to a daring mission. The Delta force had months before been transported to the Middle East, and then had been psychologically let down when it was sent home. When satellite communication insured that the decision on whether or not to abort the mission would be made in the Oval Office rather than in the field, the spirit of caution took over.

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I just finished reading the March issue of Defense/80, a publication of the Defense Department. The issue is entitled, "The Soviet March Towards Technological Superiority." To put it bluntly, it is a frightening issue, and the facts and conclusions here are well documented. Perhaps the worst part of the picture is the statement: "The Soviet Union has negotiated such agreements with a large number of US companies....who are 'front-runners' in areas in which the Soviets are deficient. There is no

formal US government oversight on these agreements unless the accord results in the sale or transfer of an item or technical data that requires a validated export license. We view these agreements as still another mechanism for the potential transfer of advanced technology." As someone once said, "Treason is simply a matter of TIMING."

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I'll be traveling East on June 3 to speak at the big NCMR Conference in Montreal . This one, like all NCMR conferences, should be a winner (write to 8422 Oak St., New Orleans, LA 70118 for info). But before hitting Montreal, I am stopping off at NYC to see the great Picasso exhibit at the Museum of Modern Art. Picasso, to my mind, will go down as one of the towering geniuses of the twentieth century.

Did you ever stop to think that great art outlasts almost everything else. It's the highest expression of the human spirit. We all know about Rembrandt, but who was ruler of Holland when Rembrandt painted? Who were the great public figures during Shakespeare's time? Who was running France when Cezanne first started painting? The works of the great artists never die. But the memories of their peers fade away, as does much of the history of their times.

* *

Insiders say that if this were not an election year, Chrysler would be allowed to go under. The feeling is that even with a huge loan package, Chrysler will probably not make it through 1981. Treasury Secretary Miller has been putting tremendous pressure on Chrysler's banks to get its revised loans through, and the main reason is that the Administration does not want an historic bankruptcy before the November election. Politics is a wonder, isn't it?

INTUITION: During the 19th Century there was a great materialistic movement linked with a scientific wave which led men to believe only what they could see with their own eyes or what they could explain through science. The new gods were rationalism and science, and this probably led the way to acceptance of such revolutionary theories as Darwin's evolution of the species and Freud's theory of the unconscious and Einstein's theory of relativity.

Today, we see a new eclecticism. With the rise of the Age of Aquarius, people seem more ready to delve into psychic phenomena. Leading scientists are talking about areas that they believe are more metaphysical than physical. The search for what lies within shares equal billing with the search for what lies "out there."

Occasionally, I read something that confirms my own belief that "all life is a school, and each day provides the lessons." The teachers, I firmly believe, are the powers above, and our job is to advance our own souls (and to help others) by mastering the lessons that are provided us.

The following remarkable story comes from an article entitled "Dreams" from the current issue of the magazine, *Science Digest*. I suppose you could say that this story is explainable through a series of uncanny coincidences. I, however, have long since given up the idea that there is any such thing as a "coincidence." In my opinion, every coincidence is (in reality) a lesson. You either learn from it or you don't. As I see it, Mr. Morris must have been "told" over and over again to *follow his hunches, his intuitions, his dreams.* When he failed again, the powers above gave up on him, but decided to make a lesson out of his tragic death. It's a lesson you can learn now:

> More remarkable still—in fact perhaps the most astonishing of all prophetic dreams ever published—must be that of Robert Morris, father of "the financier of the American Revolution," who dreamed he himself was destined to be shot to death by one of the big guns on a naval vessel he was scheduled soon to visit. Because of the dramatic vividness of his dream, he felt apprehensive about the ship and tried to cancel his visit, but naval officers told him he was being absurd, if not cowardly, and eventually the ship's captain convinced him that it was absolutely safe to go aboard as no guns would be fired until after he left. At the end of his visit, the captain tried to make good on this promise by ordering that a salute (without a cannonball) be fired only after he raised his hand when the party, including Morris, had safely reached shore. But while the boat was still within gun range, a fly alighted on the captain's nose, causing him to raise his hand to brush it off. And the ship's gunner, taking this as the signal to fire, fired with the astounding result that a tiny fragment of the discharge hit Morris and wounded him fatally!

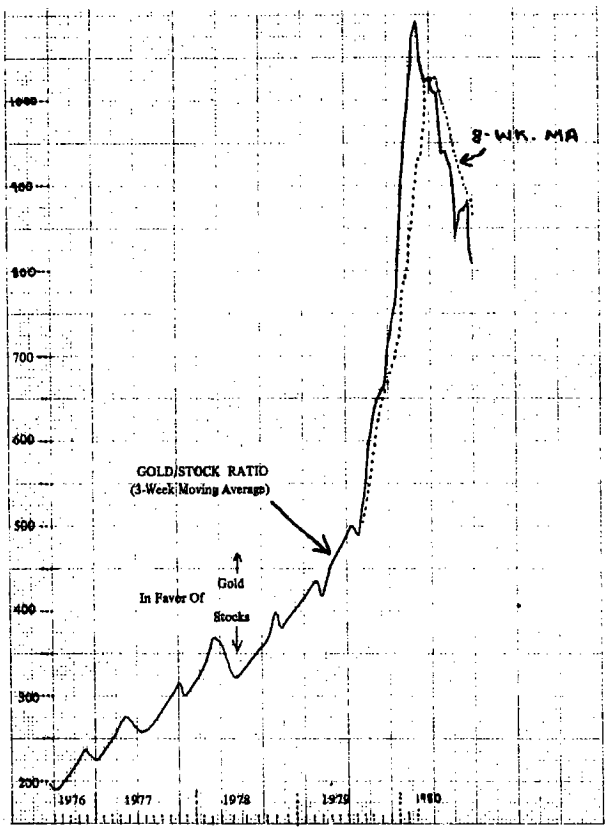
GOLD/STOCK RATIO: In Letter 777 (under "Three Important Developments") I noted that "my gold/stock ratio is now running in favor of stocks," and I added that the 3-week moving average of this ratio is about to drop under the 8-week MA." I don't know if many subscribers took this seriously, but the results of this trend are beginning to emerge now.

What we see here is a ratio of gold divided by the NYSE Composite Index. The black line is a 3-week MA of the ratio while the dotted line is an 8-week MA of the ratio. On the week of February 6 the 3-week MA turned down. This meant that stocks were definitely out-performing gold on a relative strength basis. Since gold was still "hot" at that time and stocks were definitely "cool," this drop in the ratio did not seem particularly significant. But I noted that after a three year rising trend in the ratio, the potential could be very significant.

On the week of March 20 the 3-week MA broke below the 8-week MA. This was the signal for a major change. The ratio (actually, the markets) were telling me that on a relative basis, stocks (for the first time since 1976) were out-performing gold in a very important way. I cautioned that this did not mean that stocks had to go up. It was a relative strength signal, and as such it could also mean that both stocks and gold could decline, but that stocks would decline LESS than gold.

Please note that the 3-week MA turned down before the Hunt disaster, before the silver collapse. The cycle of precious metal

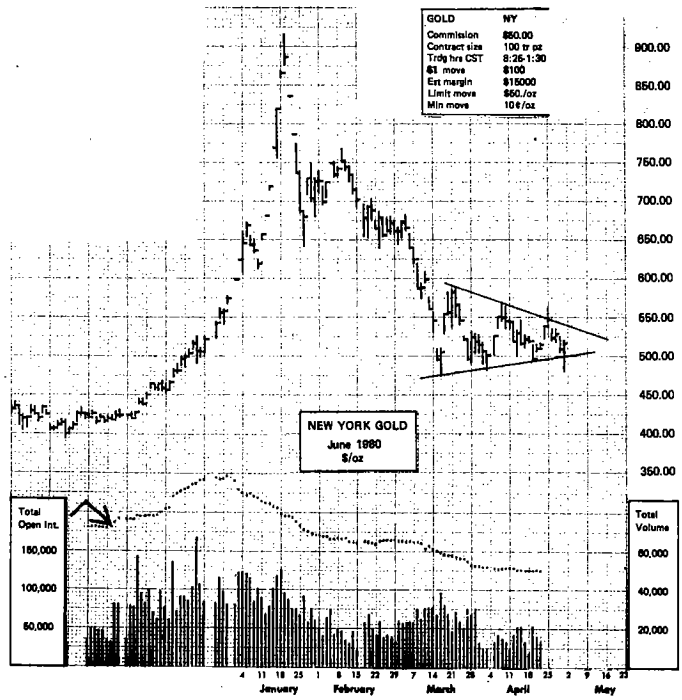
strength ENDED well before any silver news. The Hunts simply got caught in the down-cycle! I expect this cycle of superior relative strength in stocks to last for quite a while, perhaps for 6 months to a year (possibly even longer). In the meantime, I will watch the ratio carefully. When it finally turns up again, it should provide a good signal for a move into gold again.



GOLD, SILVER: The facts about the great Hunt "silver corner" are beginning to surface, and one thing is sure–old daddy H.L.Hunt (who made the money in the first place) would never have approved. In fact, if H.L. were alive today, I'd bet there'd be "f'ar 'n brimstone" flying down in Texas. Nobody knows how high the Hunt silver pyramid went, but one thing is obvious–the losses are staggering. In fact, when it's all over it wouldn't surprise me to learn that the two Hunt brothers are well down on the list of the richest men in the Lone Star State. But you can bet on one thing–the boys are a lot older and a lot wiser than they were a few months ago.

Fed Chairman Volcker isn't happy about the whole affair either, and it sounds as if before the final bank loans are made, the Hunts will be forced to agree to stay out of commodities forever. Well, the only point I'm trying to get across to my subscribers is this–if you're out to corner a market, make sure you have a lot of cash around to back you up. Otherwise, you may go through the wringer, and for what? "Who needs it!" as they so quaintly put it in Gotham.

During all the hoop-la, gold has not been doing an awful lot. In fact, the daily movements of gold since March have been tracing out a very pretty symmetrical triangle (see daily chart, courtesy of my friends at Dunn & Hargitt, 22 N. Second, Lafayette, Ind. 47902). When the price movement traces out



a symmetrical triangle, usually the longer the elapsed time prior to the ultimate triangle breakout, the weaker the move. Note that the price movement has continued practically to the apex of the triangle. Thus, most of the potential upward "oomph" has probably been expended. It would not surprise me to see a final upward pop, however, but I would be skeptical of a continuing rally. Such formations often end with a final deceptive rally out of the triangle apex–and then a spill to the downside.

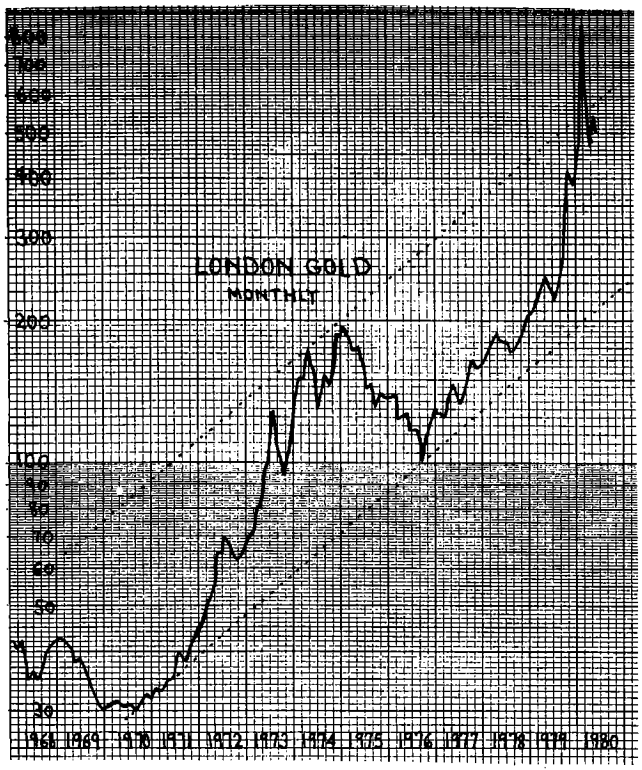
Note the decline in the open interest in the June Gold contract. Traders have been leaving the scene. The cost of carrying gold has been too high, particularly in this trendless market. I'd say that June gold would have to hit 600 to look good. On the other hand, a break below 465 on June gold would look like the start of a voyage to the lower depths, probably to the mid to lower 300's.

I was not impressed with gold's action during the ill-fated Carter rescue attempt in Iran. The newspapers made the whole tragic scene look like thebeginning of World War III and gold still could not close above the upper trendline of the triangle. My feeling was that if the Iranian Rescue had occurred say last year (when gold was in a strongly bullish trend) the metal would have jumped $200 overnight. Recently, I've had the feeling that "someone" is taking every rally in gold as a chance to unload, but maybe not, maybe I just don't see the picture.

To gold's credit, it also seems like somebody is picking up the metal every time it breaks 500. And that's what makes horse races–and symmetrical triangles.

From the long-term picture, my ratio chart shows gold back within its giant rising channel. The picture looks as though gold "should" ultimately correct back to at least the middle of the channel (around 350-400), but the longer the elapsed time with gold holding above 480-500, the more hopeful for the technical picture.

Silver obviously blew its primary top when it hit 50, following which it crashed down to below 11. I mean, that's a total collapse



and such things only happen when the primary trend of an item is down. It's hard for me to believe that silver is in a primary bear market while gold remains bullish, but these are strange and perilous times and I suppose we should be ready to accept anything (after all, which of us old-time gold bugs ever thought we'd see gold above 500 in the first place!).

The exponential moving averages for gold are short-term bearish and longer term still bullish. The 5-week MA is at 519, well under the 13-week MA which stands at 551. But the long-term or 50-week MA for gold is at 461 and is climbing at the rate of about 2 points per week. From my experience with these moving averages, I would say that to turn bearish in a primary way, I would want to see spot gold plunge below 461 and stay there–and that hasn't happened yet.

I'm going to express an opinion here on gold–but remember, this is just my opinion, nothing more. Often when an item (gold, a stock, any tradeable item) holds to a trading range following a major decline, you will see one final downward plunge prior to formation of an important bottom. That's the feeling I get about gold now.

I believe that one final "cleanout" plunge in gold would take the metal to an important bottom area, and in that case new buying, important buying, would be in order. Walt Bressert of HAL Commodity Cycles has probably done as much work on commodity cycles as any man in the nation (HAL Commodity Cycles, PO Box 40070, Tucson, AZ 85717). Walt called the 5½ year cycle top for silver perfectly this year when he stated in 1979 that silver was slated for a major top in the first quarter of 1980.

Now Walt is talking about an important cycle low for gold and silver in June (next month). I won't argue with Walt about the exact month, but a final descent does fit into my own theory about how the gold picture could go. If it's June, well that would be a beautiful second cyclical call for Walt. At any rate, watch the 460 spot level for gold. Watch June. If gold breaks 460, I believe it will be in its final leg down, and I will be a buyer at the end of that leg.

LATE STOCK MARKET NOTES: This just isn't an easy business. No sooner did I write about the "lagging Transports" when those laggards jumped a fat 5.41 points on May 2, taking them within 5.94 of their April peak (the April peak was 255.46). If the market can muster enough strength to take the Transports over the 253.46 level, the non-confirmation will have been erased and the technical picture will appear much stronger.

In the meantime, market breadth appears tired, and the daily new highs are still under 20. The underlying technical condition of this market still does not impress me, and I happen to think it's a typical bear market rally.

I also believe that the collapse in interest rates is exerting a very positive influence on Wall Street. But interest rates don't collapse out of nowhere. They're caving in now because business is turning bad almost faster than the newspapers can report the statistics. I expect business to be in shambles by mid-summer, and what fascinates me is the manner in which this market may discount the deepening recession.

MEAN: I suppose you could call this a "mean cartoon," but "I'm mad as hell, and I'm not gonna take it any more!" Anyway, I feel a bit mean, so I'm including this cartoon, and if Carter doesn't approve, well let him switch to somebody else's market report.

NEXT MAILING: May 21st